IN THE

Supreme Court of the United States

OCTOBER TERM, 1973

No. 73-5265

HENRY A. KOKOSZKA,

Petitioner,

—v.—

RICHARD BELFORD, Trustee in Bankruptcy of the Estate of Henry A. Kokoszka, Bankrupt,

Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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RELEVANT DOCKET ENTRIES

Date	Docket Entry
1- 5-72	Petition and Schedules, filed at 3:12 p.m.
2- 3-72	Referee's order re income tax refund
2- 7-72	Motion for Rehearing
3-24-72	Referee's order on Motion for Rehearing
4- 3-72	Petition for Review filed
4-11-72	Certificates of Referee on Petition for Review filed
7-24-72	Memorandum of Decision filed and entered. The Petition for Review is denied and the order of the Referee is confirmed. (Newman, J.)
8-21-72	Petition for Allowance of Appeal filed
8-21-72	Motion for leave to proceed in forma pauperis
9- 5-72	Petition for allowance of appeal granted
9- 5-72	Motion for leave to proceed in forma pauperis granted
5-18-73	Appeal affirmed in part; reversed in part

UNITED STATES DISTRICT COURT
DISTRICT OF CONNECTICUT

In Bankruptcy

No. 37437

In the Matter of

HENRY ANTHONY KOKOSZKA, BANKRUPT

ORDER RE INCOME TAX REFUND AND DEFERMENT OF BANKRUPT'S DISCHARGE

It appearing that the bankrupt may be entitled to an income tax refund from Internal Revenue Service on taxes withheld from wages or otherwise paid prior to bankruptcy, it is

ORDERED that:

(a) the bankrupt shall promptly file with the trustee in bankruptcy a copy of his income tax return for the year 1971 if it has now been prepared, or shall do so as soon as the return is prepared;

(b) the bankrupt shall do all things requisite to assist the trustee in bankruptcy in recovering any such refund;

(c) the bankrupt shall forthwith deliver to the trustee in bankruptcy any tax refund that may be paid to the bankrupt;

(d) the trustee in bankruptcy shall promptly notify Internal Revenue Service of his right to any tax refund now or eventually due to the bankrupt; and,

(e) entry of the bankrupt's discharge in bankruptcy, if eventually he be entitled thereto, shall be deferred until the bankrupt has complied with this order.

Dated at Bridgeport, February 3, 1972

R. E. TREVETHAN
Referee in Bankruptcy

UNITED STATES DISTRICT COURT
DISTRICT OF CONNECTICUT

[Title Omitted]

MOTION FOR REHEARING

The petitioner herein moves that this court grant a rehearing with regard to its order of February 3, 1972, directing that the bankrupt turn over his tax refund to the trustee in bankruptcy. The petitioner wishes to present evidence as to the amount of income withheld, the reasons therefor, and the employment record of petitioner.

Upon hearing said evidence, petitioner requests that the order of February 3, 1972 be vacated for the following reasons:

1. Said tax refund is not "property" within the meaning of sections 70a(5) and 70a(6) of the Bankruptcy Act. *Frederick* v. *Lines*, 400 U.S. 18 (1970).

2. Said tax refund is not so rooted in the pre-bankruptcy past as to constitute property within the meaning of sections 70a(5) and 70a(6) of the Bankruptcy Act, or *Segal* v. *Rochelle* et seq. 382 U.S. 375 (1966).

3. Said order is inconsistent with the purposes of the Bankruptcy Act in that it hinders the bankrupt from an unencumbered fresh start.

4. Said tax refund is the equivalent of future wages.

THE PETITIONER

By:

FRANCIS X. DINEEN
His Attorney

[Certificate of Service Omitted in Printing]

UNITED STATES DISTRICT COURT
DISTRICT OF CONNECTICUT

In Bankruptcy

No. 37437

In the Matter of

HENRY ANTHONY KOKOSZKA, BANKRUPT

ORDER ON MOTION FOR REHEARING

By its customary order entered *ex parte* on February 3, 1972 this court directed the bankrupt, among other things, to turn over to the trustee in bankruptcy any tax refund he might receive on his 1971 federal income taxes. On February 7, 1972 the bankrupt filed a motion requesting a rehearing on this order and that it be vacated on the grounds that (a) the tax refund is not property within sections 70a(5) and 70a(6) of the Bankruptcy Act and case law, (b) the order is inconsistent with the purposes of the Bankruptcy Act in that it hinders the bankrupt from an unencumbered fresh start, and (c) the tax refund is the equivalent of future wages.

Duly noticed hearing was held on the motion at which the bankrupt and the trustee in bankruptcy appeared. The evidence offered at the hearing is as follows. The bankrupt was employed for approximately the first three months of 1971, was unemployed from April, 1971 to late December, 1971 and received unemployment compensation, and then was reemployed and worked about the last week and a half of December, 1971. During the year 1971 the bankrupt had two exemptions for federal income tax purposes, and the bankrupt told his employer that he was taking his two exemptions on the tax withholdings from his pay.

The bankrupt's federal income tax return for 1971 sets forth that he is entitled to a tax refund of $250.90. Presumably, this refund arises because the periodic withholdings from the bankrupt's pay were under a tax table geared to total annual compensation which was more than the bankrupt actually earned.

The bankrupt needs either an operation for a hernia or some form of abdominal supporter, dental work and he could use eyeglasses for distance when walking. His wife has not worked in the past twenty four years.

Until recent days it was thought "firmly established that the bankruptcy trustee succeeds to any claim or right of action the bankrupt may have against the Government for a refund of taxes paid" (4A *Collier*, Bankruptcy, par. 70.28(4) and authorities cited in note 27). Consistent with this concept, a trustee in bankruptcy acquires title to a claim a bankrupt may have for a tax refund based on the loss-carryback provisions of the Internal Revenue Code when applied to taxes paid by a bankrupt prior to bankruptcy (*Segal* v. *Rochelle*, 1966, 382 U.S. 375). But, in view of the recent case of *Lines* v. *Frederick*, 1970, 400 U.S. 18, the bankrupt here claims that a tax refund arising out of an excess of tax withholding by an employer from the wages of a bankrupt-employee remains the property of the employee and does not pass to the trustee in bankruptcy.

The *Lines* case involved the question of whether a bankrupt wage earner's vacation pay, accrued but unpaid at the time of bankruptcy, passes to the trustee in bankruptcy as property under section 70a(5) of the Bankruptcy Act or remains the property of the bankrupt. The court reviewed the *Segal* case, *supra*, and commented that the tax refund claim in that case arose out of business operations and was "sufficiently rooted in the pre-bankruptcy past and so little entangled with the bankrupt's ability to make an unencumbered fresh start that it should be regarded as 'property' under sec. 70a(5)". The court then proceeded as follows:

> By contrast, the respondents here are wage earners whose sole source of income, before and after bankruptcy, is their weekly earnings. The function of their accrued vacation pay is to support the basic requirements of life for them and their families during brief vacation periods or in the event of layoff. Since it is a part of their wages, the vacation pay is "a specialized type of property presenting distinct problems in our economic system" (case cited).

> Where the minimal requirements for the economic survival of the debtor are at stake, legislatures have recognized that protection that might be unnecessary or unwise for other kinds of property may be required . . . .
>
> The wage-earner bankrupt who must take a vacation without pay or forego a vacation altogether cannot be said to have achieved the "new opportunity in life and (the) clear field for future effort, unhampered by the pressure and discouragement of preexisting debt," (case cited) which it was the purpose of the statute to provide.

To resolve the issue here presented requires an analysis of the *Lines* case in the light of the basic statutory law and the *Segal* case.

A trustee in bankruptcy is vested by operation of law with the title of the bankrupt as of the date of bankruptcy to property, including rights of action, which prior to bankruptcy the bankrupt could have transferred by any means (Bankruptcy Act, sec. 70a(5)55. In *Segal* the court observed that:

> The main thrust of section 70a(5) is to secure for creditors everything of value the bankrupt may possess in alienable or leviable form when he files his petition. To this end the term "property" has been construed most generously and an interest is not outside its reach because it is novel or contingent or because enjoyment must be postponed.

The court also remarked that, on the other hand, one highly prominent purpose of the Bankruptcy Act "is to leave the bankrupt free after the date of his petition to accumulate *new* wealth in the *future* (underlining added)." It then concluded that the loss-carryback refund claim was "sufficiently rooted in the pre-bankruptcy past and so little entangled with the bankrupts' ability to make an unencumbered fresh start that it should be regarded as 'property' under section 70a(5)."

Returning to the *Lines* case we must now endeavor to extract from the essentials of what was there said—already set forth earlier in this opinion—the basic and

controlling concept which it pronounces. As this court analyses it, *Lines* laid down the precept that an exception from the impact of section 70a(5) must be judicially carved out for accrued vacation pay because of its *prospective purpose* as *future support* for the wage-earner's basic requirements for living and caring for his family during vacations or a layoff. To take away his accrued vacation pay, specifically designed and intended for the future acquisition of the necessities of life during a period when the wage-earner was not at his labor, would be tantamount to an appropriation by a trustee in bankruptcy of what in fact had all the flavor of future wages acquired after bankruptcy. Thus, as this court views it, *Lines* rests upon the thought that wages earned and held specifically for the future support of the bankrupt and his family during a foreseeable period away from daily labor should be held for that purpose insulated from alienation by creditors.

It is this court's belief that there are such marked differences between the nature of a claim to a tax refund and that of accrued vacation pay as evolved by *Lines* that the concept of *Lines* cannot logically or sensibly be extended to embrace a claim to a tax refund as a further judically conceived exception to section 70a(5) of the Act. First, wages are withheld under federal law for application on an eventual tax liability and are paid to and become the property of the government. Second, the wages are not withheld for taxes under any designed program that they or any portion of them shall be returned to the bankrupt to insure his future support when he is without daily earnings. Third, a claim to a refund arising out of taxes voluntarily or involuntarily paid out of wages is quite the equivalent of savings accumulated by a bankrupt out of his yearly earnings and any such savings held by a bankrupt at bankruptcy—whether in the form of cash in a safe deposit box or in a bank account—became the property of the bankruptcy estate. Fourth, a claim to a refund is not distinguishably different from any other property or property right which a bankrupt might have acquired by using a portion of his annual wages to make a loan to another, to buy se-

curities or to acquire an automobile, all of which pass to a trustee in the event of bankruptcy. Accordingly, it is the view of this court that a claim to a tax refund for excess taxes paid from wages is quite something different from a right to receive accumulated wages in the future which were specifically designed to substitute for future lack of earnings. The concept of *Lines* is not applicable to a tax refund. Such a refund is a property which passes to a trustee in bankruptcy under section 70a(5).

This court also finds unacceptable the contention that a distinction is to be drawn between a claim for tax refund based on wages withheld in the amounts fixed by the federal tax withholding tables and a claim wholly or partially resulting from withholdings in excess of the amounts required by the tax tables. One court has seen fit to draw this distinction (*Matters of Cedor and James*, #2-70 287 ACW and #3-70 1064 ACW, D.C.N.D. Calif., 1/20/72). However, flowing from all which this court has already said in this opinion, it is its conclusion that a claim to a tax refund, however it may have been created, is quite something different from, and does not fall within the ambit of, the concept of accrued vacation pay as developed in the *Lines* case.

Finally, it is the view of this court that the wage garnishment provisions of the Consumer Credit Protection Act (Consumer Act) (15 USC sec. 1671 *et seq*) do not have any impact to limit a bankruptcy estate to 25% of a tax refund and to give the bankrupt 75% thereof. This court is compelled to disagree with the contrary position taken in the *Matters of Cedor and James, supra.*

Reading the Consumer Act as a cohesive entity, it is concluded that its sole purpose and effect is restricted to wage garnishment procedures as they have been historically understood to limit to 25% the amount that periodically may be taken from a person's current and future weekly take-home pay to be applied against an indebtedness. The opening section of the Consumer Act (15 USC sec. 1671) sets forth the findings of Congress that "unrestricted garnishment of compensation due for

personal services" encourages extension of credit, and that the "application of garnishment as a creditor's remedy frequently results in loss of employment by the debtor". Encouragement of credit and loss of employment may result from the normal wage garnishment which regularly takes a portion of a debtor's pay as it falls due. This court cannot conceive that either can result from the passage of a debtor's tax refund to his bankruptcy estate.

The next section of the Consumer Act (15 USC sec. 1672) defines "garnishment" to mean "any legal or equitable procedure through which the earnings of any individual are required to be withheld for payment of any debt", and the term "earnings" means "compensation paid or payable for personal services". These definitions demonstrate that under the Consumer Act wage garnishment procedure means what it has historically meant; it means a repetitious withholding of money from the debtor's periodic earnings for application on a debt. The claim of a trustee in bankruptcy to a bankrupt's tax refund is not a withholding of the bankrupt's earnings; the withholding occurred when the monies were taken from the bankrupt's pay to apply on his taxes. Certainly, the tax refund arises out of a use previously made of a portion of the bankrupt'a past pay, but so do property rights in stocks, bonds, automobiles or anything else acquired with previous earnings. And, surely, it would not be rational to say that a trustee's succession to these properties of a bankrupt constitute a garnishment of his earnings within the framework of the Consumer Act.

It is also provided in the Consumer Act that "disposable earnings" means that "part of the earnings of any individual remaining after the deduction from those earnings of any amounts required by law to be withheld" (15 USC sec. 1672) and that "the maximum part of the aggregate disposable earnings of an individual *for any workweek* which is subjected to garnishment may not exceed 25 per centum of his disposable earnings *for that veek* (underlining added)" (15 USC sec. 1673). It might be enough to say that here what created the claim to a tax refund was not the "disposable earnings"

of the bankrupt but the deductions from his earnings of amounts required by law to be withheld under the federal withholding tax tables. Thus, the 25% limitation on disposable earnings has no application to the earnings which created the refund. Moving to a broader view of these portions of the statute, it is apparent from the express provisions that their purpose and effect is to limit to 25% of the disposable earnings *for any workweek* the amount that may be taken by garnishment *for that week.* Such clear language compels its conclusion that the 25% limitation of the statute has application only to the amount that can be taken weekly from a debtor's pay under normal garnishment. This court finds it impossible to distort such specific language to extend it to include 25% of any claim a bankrupt may have against the government for a tax refund.

The next section of the Consumer Act (15 USC 1674) provides that "no employer may discharge any employee by reason of the fact that his earnings have been subjected to garnishment for any one indebtedness." Human experience tells us that this relates to the past practice of many employers who would discharge garnished employees because of their improvident ways and to avoid the necessary bookkeeping involved in honoring even a single weekly garnishment. Certainly, that a trustee may have a right to a bankrupt's tax refund is unrelated to personal improvidence and cannot result in the imposition of any conceivable burden upon an employer which would precipitate discharge of the employee.

And, finally, it is this court's view that—contrary to the thinking expressed in the *Matters of Cedor and James, supra,*—the provision of the Consumer Act that the 25% limitation does not apply to "any order of any court of bankruptcy under Chapter XIII of the Bankruptcy Act" cannot be interpreted to mean that the 25% limitation does embrace a tax refund. This provision relates to section 658 of Chapter XIII which gives the bankruptcy court the power to order the employer of a Chapter XIII debtor to withhold from the bankrupt's pay and turn over to the trustee whatever periodic amounts the debtor has agreed to pay to the trustee

under the terms of his wage-earner plan. It expressly leaves this judicial power unaffected by the 25% limitation on periodic withholdings from the debtor's earnings, and it has no other effect.

All in all, if a wage-earner's right to a tax refund is to be excepted from the provisions of section 70a(5) of the Bankruptcy Act, it is for Congress and not judicial authority to accomplish it.

In view of all that has been said, it is

ORDERED that the bankrupt's motion to vacate this court's order of February 3, 1972 is denied.

Dated at Bridgeport, March 24, 1972.

R. E. Trevethan
Referee in Bankruptcy

UNITED STATES DISTRICT COURT
DISTRICT OF CONNECTICUT

[Title Omitted]

PETITION FOR REVIEW

TO THE HONORABLE R. E. TREVETHAN, REFEREE IN BANKRUPTCY

The petition of Henry Anthony Kokoszka, Bankrupt herein, respectfully shows:

I

That your petitioner is the Bankrupt in the above-entitled proceedings.

II

That on the third day of February, 1972, this Court made and entered an Order directing that the bankrupt deliver to the trustee in bankruptcy any tax refund now due to the bankrupt; and further ordering that entry of the bankrupt's discharge in bankruptcy be deferred until compliance with said order. A copy of the complete text of said order is annexed hereto as Exhibit A and made a part hereof as though fully recited herein.

III

That on the 24th day of March, 1972, this Court, after rehearing, denied bankrupt's motion to vacate the Court's order of February 3, 1972.

IV

That your petitioner is aggrieved by said Orders and said Orders are in error in the following respects:

1. Said tax refund is not property within the meaning of §§ 70a(5) and 70a(6) of the Bankruptcy Act. *Frederick v. Lines*, 400 U.S. 18 (1970).

2. Said tax refund is not so rooted in the pre-bankruptcy past as to constitute property within the meaning of §§ 70a(5) and 70a(6) of the Bankruptcy Act, or *Segal* v. *Rochelle*, 382 U.S. 375 (1966).

3. Said order is inconsistent with the purposes of the Bankruptcy Act in that it hinders the bankrupt from an unencumbered fresh start.

4. Said tax refund is the equivalent of wages.

5. Under the Federal Consumer Credit Protection Act, the trustee is not entitled to more than 25% of the bankrupt's tax refund.

WHEREFORE, your Petitioner prays that a certificate be promptly prepared as required by law and forwarded to the Clerk of the United States District Court and that upon the hearing thereof, said Order be reversed and petitioner's bankruptcy be allowed to proceed without payment over to the trustee of his income tax refund.

THE PETITIONER

By: FRANCIS X. DINEEN

[Certificate of Service Omitted in Printing]

UNITED STATES DISTRICT COURT
DISTRICT OF CONNECTICUT

In Bankruptcy

No. 37437

In the Matter of

HENRY ANTHONY KOKOSZKA, BANKRUPT

To The Judges Of The District Court Of The United States For The District Of Connecticut.

CERTIFICATE OF REFEREE ON
PETITION FOR REVIEW

R. E. Trevethan, the Referee in Bankruptcy in charge of this proceeding, does hereby certify all that is hereafter set forth.

On February 7, 1972 the bankrupt filed a motion requesting a rehearing on the *ex parte* order entered by this court on February 3, 1972 and that the order be vacated. That order, among other things, directed the bankrupt to turn over to the trustee in bankruptcy any tax refund he might receive on his 1971 federal income taxes. Hearing was held on the bankrupt's motion and on March 24, 1972 order entered denying the bankrupt's motion to vacate the order of February 3, 1972. On April 3, 1972 the bankrupt filed a petition for review of the order of March 24, 1972.

There is hereafter set forth a statement of the questions presented, the findings of the court, its conclusions of law, the order entered by the court and a summary of the evidence. There is submitted herewith (a) the *ex parte* order of this court dated February 3, 1972, (b) the bankrupt's motion for rehearing on this order and that it be vacated, (c) the order of this court denying the motion to vacate, (d) the bankrupt's petition for review, and (e) the single exhibit in evidence.

STATEMENT OF QUESTIONS PRESENTED

The questions presented are as follows:

1. Whether a federal income tax refund of a bankrupt wage earner which resulted from an excess of withholdings from his wages under the tax tables is a property which passes to the trustee in bankruptcy, or whether it remains the property of the bankrupt.

2. If the bankruptcy estate does have some right to such tax refund, whether it is limited to receiving only 25% of the refund under the garnishment provisions of the federal Consumer Credit Protection Act.

FINDINGS OF FACT

1. This bankruptcy proceeding was commenced by voluntary petition filed by the bankrupt on January 5, 1972.

2. On February 3, 1972 this court entered its customary *ex parte* order which, among other things, direct the bankrupt to turn over to the trustee in bankruptcy any tax refund the bankrupt might receive on his 1971 federal income taxes.

3. The bankrupt was employed for approximately the first three months of 1971, was unemployed from April, 1971 to late December, 1971 and received unemployment compensation during this period, and was then re-employed and worked about the last week and a half of December, 1971.

4. During the year 1971 the bankrupt had two exemptions for federal income tax purposes, and he told his employer that he was taking his two exemptions on the tax withholdings from his pay.

5. The bankrupt's federal income tax return for 1971 sets forth a claim to a tax refund of $250.90, and presumably this refund arises because the periodic withholdings from the bankrupt's pay were under a tax table geared to a total annual compensation which was more than the bankrupt actually earned.

6. The bankrupt's wife has not been employed during the past twenty four years.

7. The bankrupt needs either an operation for a hernia or some form of abdominal support, dental work and he could use eyeglasses for distance when walking.

CONCLUSIONS OF LAW

The conclusions of law reached by this court are fully set forth in its opinion and order of March 24, 1972 which is submitted herewith and in their essentials they may be summarized as follows:

1. The claim of a bankrupt wage earner to a federal income tax refund on taxes withheld from his earnings by his employer is not in the nature of future wages designed for the support of the bankrupt and his family, but is a property or right of action of the bankrupt which passes to the trustee in bankruptcy under the express provisions of section 70a(5) of the Bankruptcy Act.

2. It is not material whether the claim to a tax refund results from compulsory withholdings from the bankrupt's pay in the amounts fixed by the federal withholding tax tables, or whether the refund arises because the bankrupt voluntarily directed his employer to withhold more from his pay than the tax law required.

3. The garnishment provisions of the federal Consumer Credit Protection Act have no impact on the right of a bankruptcy estate to a tax refund of the bankrupt and do not limit the bankruptcy estate to 25% thereof, leaving the bankrupt with 75% of the refund.

ORDER

The order entered by this court was as follows:

"ORDERED that the bankrupt's motion to vacate this court's order of February 3, 1972 is denied."

SUMMARY OF EVIDENCE

The only testimony offered was that of the bankrupt and all of it—except for his testimony that an accountant prepared his tax return—is set forth above in the

Findings of Fact. Accordingly, there is no evidence to be summarized.

The only exhibit (Bk's Ex. A) is the bankrupt's federal income tax return for the year 1971.

Dated at Bridgeport, April 7, 1972.

R. E. TREVETHAN
Referee in Bankruptcy

13 WILLIAM STREET
WALLINGFORD, CONN. 06-0796341

WAGE AND TAX STATEMENT—1971
(Use as State or City authorizing combined form)
Employer's State identification number

Copy C—
For employee's records

Type or print EMPLOYER'S Federal identification number, name, and address above.

FEDERAL INCOME TAX INFORMATION			SOCIAL SECURITY INFORMATION		STATUS	
Federal income tax withheld	Wages paid subject to withholding in 1971[2]	Other compensation paid in 1971[3]	F.I.C.A. employee tax withheld[4]	Total F.I.C.A. wages paid in 1971[1,4]	1. Single 2. Married	*
250.90	2,322.00		120.74			**

EMPLOYEE'S social security number ▶ 042-09-8432	Name of State	State Form No.	State income tax withheld
Henry Kokoszka 39 Meadow St. Wallingford, Ct.	Name of City	City Form No.	City income tax withheld

*Excludable sick pay. **Gross wages for State if different from Federal.
[1] Includes tips reported by employee. Amount is before payroll deductions or sick pay exclusion.
[2] Add this item to wages in reporting wages and salaries on your income tax return.
[3] The social security (FICA) rate of 5.2% includes .6% for Hospital Insurance Benefits and 4.6% for old-age, survivors, and disability insurance.
[4] Includes tips reported by employee.

Type or print EMPLOYEE'S name and address (including ZIP code) above.

Uncollected Employee Tax on Tips . . . $

FORM **W–2** Department of the Treasury, Internal Revenue Service

NOTICE TO EMPLOYEE.

1. **Income Tax Wa —**This statement is important. Copy B must b ad with your U.S. Income Tax Return for 1971 and Copy 2 must be filed with your State or City Income Tax Return for 1971. If your social security number, name, or address is stated incorrectly, correct the information on copies B and 2 and notify your employer.

2. **Social Security Wages.—**If your wages were subject to social security taxes, but are not shown, your social security wages are the same as wages shown under "FEDERAL INCOME TAX INFORMATION," but not more than $7,800.

3. **Credit For F.I.C.A. Tax.—**If more than $405.60 of F.I.C.A. (social security and hospital insurance) employee tax was withheld during 1971 because you received wages from more than one employer, the excess should be claimed as a credit against your Federal income tax. See instructions for your Federal income tax return.

4. A copy of this form has been sent to the Internal Revenue Service.

Form 1040 — U.S. Department of the Treasury / Internal Revenue Service — Individual Income Tax Return — 1971

For the year January 1—December 31, 1971, or other taxable year beginning ...., 1971, ending ...., 19 ....

Please print or type

First name and initial (if joint return, use first names and middle initials of both) | Last name | Your social security number

Present home address (Number and street, including apartment number, or rural route) | Spouse's social security number

City, town or post office, State and ZIP code | Occupation: Yours / Spouse's

Filing Status—check only one:

1 ☐ Single
2 ☒ Married filing jointly (even if only one had income)
3 ☐ Married filing separately and spouse is also filing. Give spouse's social security number in space above and enter first name here ▶
4 ☐ Unmarried Head of Household
5 ☐ Surviving widow(er) with dependent child
6 ☐ Married filing separately and spouse is not filing

Exemptions — Regular / 65 or over / Blind — Enter number of boxes checked

7 Yourself . . . . ☒ ☐ ☐
8 Spouse (applies only if item 2 or 6 is checked) ☒ ☐ ☐ ▶ 2
9 First names of your dependent children who lived with you .... Enter number ▶
10 Number of other dependents (from line 33) . . . ▶
11 Total exemptions claimed . . . . ▶ 2

Please attach Copy B of Forms W-2 to back

Income

Line	Description	No.	Amount	
12	Wages, salaries, tips, etc. (Attach Forms W-2 to back. If unavailable, attach explanation)	12	2322	
13a	Dividends (see pages 6 and 11 of Instr.) $........ 13b Less exclusion $........ Balance ▶ (If gross dividends and other distributions are over $100, list in Part I of Schedule B.)	13c		
14	Interest. [If $100 or less, enter total without listing in Schedule B] [If over $100, enter total and list in Part II of Schedule B]	14		
15	Income other than wages, dividends, and interest (from line 40)	15		
16	Total (add lines 12, 13c, 14 and 15)	16		
17	Adjustments to income (such as "sick pay," moving expense, etc. from line 45)	17		
18	Adjusted gross income (subtract line 17 from line 16)	18	2322	

- See page 3 of instructions for rules under which the IRS will figure your tax.
- If you do not itemize deductions and line 18 is under $10,000, find tax in Tables and enter on line 19.
- If you itemize deductions or line 18 is $10,000 or more, go to line 46 to figure tax.

Tax, Payments and Credits

Line	Description	No.	Amount	
19	Tax (Check if from: ☐ Tax Tables 1–13, ☐ Tax Rate Sch. X, Y, or Z, ☐ Sch. D, ☐ Sch. G or ☐ Form 4726)	19	none	
20	Total credits (from line 54)	20		
21	Income tax (subtract line 20 from line 19)	21		
22	Other taxes (from line 60)	22		
23	Total (add lines 21 and 22)	23	none	
24	Total Federal income tax withheld (attach Forms W-2 or W-2P to back) — 24: 250 90			
25	1971 Estimated tax payments (include 1970 overpayment allowed as a credit) — 25			
26	Other payments (from line 64) — 26			
27	Total (add lines 24, 25, and 26)	27	250	90

Bal. Due or Refund

Line	Description	No.	Amount	
28	If line 23 is larger than line 27, enter BALANCE DUE (Pay in full with return. Make check or money order payable to Internal Revenue Service) ▶	28		
29	If line 27 is larger than line 23, enter OVERPAYMENT ▶	29	250	90
30	Line 29 to be: (a) REFUNDED (Allow at least six weeks for your refund check) ▶ 250 90			
	(b) Credited on 1972 estimated tax ▶			

Foreign Accounts

31 Did you, at any time during the taxable year, have any interest in or signature or other authority over a bank, securities, or other financial account in a foreign country (except in a U.S. military banking facility operated by a U.S. financial institution)? If "Yes," attach Form 4683. (For definitions, see Form 4683.) ▶ ☐ Yes ☒ No

Under penalties of perjury, I declare that I have examined this return, including accompanying schedules and statements, and to the best of my knowledge and belief it is true, correct, and complete.

Sign here

▶ Henry Q Kokoszka — Your signature — Date

▶ Veronica R. Kokoszka — Spouse's signature (if filing jointly, BOTH must sign even if only one had income)

▶ J. J. .... — Signature of preparer other than taxpayer, based on all information of which he has any knowledge. — Date: FEB 1972

W.... Conn. — Address

Write soc. sec. no. on Check or Money Order. Attach here

Pltf. Ex A # 37437   3/8/72 KB

 Attach Copy B of Form W–2 here. ▶

PART I.—Additional Exemptions (Complete only for other dependents claimed on line 10)

32 (a) NAME	(b) Relationship	(c) Months lived in your home. If born or died during year, write B or D.	(d) Did dependent have income of $675 or more?	(e) Amount YOU furnished for dependent's support. If 100%, write ALL.	(f) Amount furnished by OTHERS including dependent.
				$	$

33 Total number of dependents listed above. Enter here and on line 10 . . . . ▶

PART II.—Income other than Wages, Dividends, and Interest

34 Business income or (loss) (attach Schedule C) 34
35 Net gain or (loss) from sale or exchange of capital assets (attach Schedule D) . . . 35
36 Net gain or (loss) from Supplemental Schedule of Gains and Losses (attach Form 4797) . . . 36
37 Pensions and annuities, rents and royalties, partnerships, estates or trusts, etc. (attach Schedule E). 37
38 Farm income or (loss) (attach Schedule F) 38
39 Miscellaneous Income
(a) Fully taxable pensions and annuities not reported on Schedule E—see instructions on page 7 . .
(b) 50% of capital gain distributions (not reported on Schedule D) .
(c) State income tax refunds (caution—see instructions on page 7) .
(d) Alimony . . . .
(e) Other (state nature and source) ....
(f) Total miscellaneous income (add lines 39(a), (b), (c), (d) and (e)) 39
40 Total (add lines 34, 35, 36, 37, 38, and 39). Enter here and on line 15 . . . . ▶ 40

PART III.—Adjustments to Income

41 "Sick pay" if included in line 12 (attach Form 2440 or other required statement) 41
42 Moving expense (attach Form 3903) 42
43 Employee business expense (attach Form 2106 or other statement) 43
44 Payments as a self-employed person to a retirement plan, etc. (attach Form 2950SE) 44
45 Total adjustments (add lines 41, 42, 43, and 44). Enter here and on line 17 . . . . ▶ 45

PART IV.—Tax Computation (Do not use this part if you use Tax Tables 1–13 to find your tax.)

46 Adjusted gross income (from line 18) 46
47 (a) If you itemize deductions, enter total from Schedule A, line 32 and attach Schedule A
(b) If you do not itemize deductions, and line 46 is:
(1) $10,000 or more but less than $11,538.43, enter 13% of line 46
(2) $11,538.43 or more, enter $1,500.
Note: deduction under (1) or (2) is limited to $750 if married and filing separately. 47
48 Subtract line 47 from line 46 48
49 Multiply total number of exemptions claimed on line 11, by $675 49
50 Taxable income. Subtract line 49 from line 48 . . . . ▶ 50

(Figure your tax on the amount on line 50 by using Tax Rate Schedule X, Y or Z, or if applicable, the alternative tax from Schedule D, income averaging from Schedule G, or maximum tax from Form 4726.) Enter tax on line 19.

PART V.—Credits

51 Retirement income credit (attach Schedule R) 51
52 Investment credit (attach Form 3468) 52
53 Foreign tax credit (attach Form 1116) 53
54 Total credits (add lines 51, 52, and 53). Enter here and on line 20 . . . . ▶ 54

PART VI.—Other Taxes

55 Self-employment tax (attach Schedule SE) 55
56 Tax from recomputing prior-year investment credit (attach Form 4255) 56
57 Minimum tax (see instructions on page 8). Check here ☐, if Form 4625 is attached 57
58 Social security tax on unreported tip income (attach Form 4137) 58
59 Uncollected employee social security tax on tips (from Forms W–2) 59
60 Total (add lines 55, 56, 57, 58, and 59). Enter here and on line 22 . . . . ▶ 60

PART VII.—Other Payments

61 Excess FICA tax withheld (two or more employers—see instructions on page 8) 61
62 Credit for Federal tax on special fuels, nonhighway gasoline and lubricating oil (attach Form 4136) . 62
63 Regulated Investment Company Credit (attach Form 2439) 63
64 Total (add lines 61, 62, and 63). Enter here and on line 26 . . . . ▶ 64

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UNITED STATES DISTRICT COURT
DISTRICT OF CONNECTICUT

Bankruptcy No. 36,028

In the Matter of

HERBERT E. SANDS

Bankruptcy No. 36,197

In the Matter of

FRANK O'BRIEN

Bankruptcy No. 37,437

In the Matter of

HENRY KOKOSZKA

MEMORANDUM OF DECISION

The common substantive issue in these three separate petitions, seeking review of decisions of a Referee in Bankruptcy, is whether an income tax refund paid to a bankrupt who claimed, for withholding purposes, all of the exemptions to which he was entitled, is property within the meaning of § 70(a)(5) of the Bankruptcy Act, 11 U.S.C. § 110(a)(5). If so, the refund vests in the Trustee and is available to the creditors. Kokoszka also contends that if the refund is such property, it is subject to the garnishment provisions of the Consumer Credit Protection Act, 15 U.S.C. §§ 1601 *et seq.*

Kokoszka's petition seeks review of the Referee's decision of March 24, 1972, refusing to vacate an order previously entered on February 3. That order requires the bankrupt to turn over to the trustee in bankruptcy any refund he may receive from the payment of his 1971 federal income taxes. Similar orders were issued in the cases of Sands and O'Brien. It is not at all clear that the orders in their cases may now be attacked since, unlike Kokoszka, they did not seek review of the Referee's

tax refund order when made, but instead received and spent their refunds and thereafter sought to challenge the order by a motion to vacate in the face of a trustee's motion to deny discharge. However, Kokoszka's petition properly brings the merits of the dispute to this Court, and the decision as to his claims disposes of the other cases as well.

The issue on the merits in all three cases is whether an income tax refund has been exempted from the definition of property in the Bankruptcy Act by the rationale of the decision of the Supreme Court in *Lines* v. *Frederick*, 400 U.S. 18 (1970). In addition to Referee Trevehtan's thoughtful opinions rejecting the petitioners' contentions in these cases, the issue has been resolved against the position of the bankrupts by a District Judge in *In re Jones*, No. 4-69 Bky. 929(o) (D. Minn. Mar. 29, 1972), *leave to appeal denied* (8th Cir. May 14, 1971), *cert. denied* —— U.S. —— (1972); and by a Referee in *In re Kingswood* (Bankruutcy No. 90279, C.D. Cal. Mar. 28, 1972), and the same result was implicit in the decision of the Eighth Circuit in *In Re Wetteroff*, —— F. 2d —— (8th Cir. Jan. 13, 1972). One District Judge has ruled in favor of the position of the bankrupts, *In re Cedor and James*, —— F. Supp. —— (N.D. Cal. Jan. 20, 1972).

The contention of the bankrupts is that a tax refund is similar to the vacation pay which was exempted from the Act in *Lines*. While there are some similarities, the critical question is whether the tax refund has those characteristics of vacation pay which were deemed pertinent to the Bankruptcy Act in *Lines*. The Supreme Court was concerned in *Lines* with the Act's purpose of enabling the bankrupt to make an "unencumbered fresh start." 400 U.S. at 20. The Court pointed out that the function of accrued vacation pay is "to support the basic requirements of life . . . during brief vacation periods or in the event of layoff." *Ibid.* The Court concluded that the bankrupt could not achieve the "new opportunity in life" which is a purpose of the Act if he must forego a vacation or take one without pay. The same simply cannot be said for an income tax refund. It is not a function

of the refund to support the basic requirements of life. That is the function of the bankrupt's regular wages. He does not forego future wages, after bankruptcy, because he loses his tax refund from previous wages. Even as to his past wages, at most he will typically lose from each week's payment a small fraction representing the excess withholding. Moreover, losing the refund is not the equivalent of foregoing a vacation or taking one without pay. Nor does it become so just because the bankrupt could elect to use the refund dollars for a vacation. By the same token he might like to use any funds he may have put aside prior to bankruptcy for a post-bankruptcy vacation, but the Act does not give him that choice.

Kokoszka also contends that some portion of his refund is immunized from the trustee by the restrictions on garnishment contained in the Consumer Credit Protection Act (CCPA), 15 U.S.C. §§ 1601 *et seq.* The restriction applies only to "disposable earnings," 15 U.S.C. § 1673, and that term is defined as "that part of the earnings of the individual remaining after the deduction from those earnings of any amounts required by law to be withheld." 15 U.S.C. § 1672(b). This definition precludes application of the CCPA to the amounts deducted in this case since all exemptions were claimed, even though it subsequently develops that some or all of those amounts are to be refunded.

In all three cases, the petitions for review are denied and the orders of the Referee are confirmed.

Dated at Hartford, Connecticut, this 21 day of July, 1972.

JON O. NEWMAN
United States District Judge

UNITED STATES DISTRICT COURT
DISTRICT OF CONNECTICUT

In Bankruptcy No. 36028

In the Matter of

HERBERT E. SANDS, BANKRUPT

In Bankruptcy No. 36197

In the Matter of

FRANK O'BRIEN, BANKRUPT

In Bankruptcy No. 37437

In the Matter of

HENRY A. KOKOSZKA, BANKRUPT

CLERK'S CERTIFICATE

I, GILBERT C. EARL, Clerk of the United States District Court for the District of Connecticut, do hereby certify that the foregoing copies of Docket Entries lettered, S.A., O.A., and K.A. and original papers numbered S1 through S8, 01 through 06, K1 through K7 and SOK 1 constitute the Record on these appeals.

And, pursuant to Rule 11(b) of the Federal Rules of Appellate Procedure, I further certify that this Record is transmitted to the Clerk of the Court of Appeals by certified mail this 13th day of October 1972.

Dated at Bridgeport, Connecticut, this 13th day of October 1972.

GILBERT C. EARL
Clerk

By: /s/ Thomas A. Grimes
THOMAS A. GRIMES
Deputy Clerk

[Filed United States Court of Appeals, Second Circuit Oct. 16, 1972, A. Daniel Fusaro, Clerk]

[SEAL]

IN THE
UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

[Title Omitted]

PETITION FOR ALLOWANCE OF APPEAL

* * * *

UNITED STATES COURT OF APPEALS
SECOND CIRCUIT

[Title Omitted]

* * * *

It is hereby ordered that the petition made herein by counsel for the appellants for allowance of appeal pursuant to Rule 6 of the Federal Rules of Appellate Procedure and Section 24 of the Bankruptcy Act (11 USC § 47) be and it hereby is granted.

/s/ Henry J. Friendly
HENRY J. FRIENDLY

/s/ J. EDWARD LUMBARD
J. EDWARD LUMBARD

/s/ Wilfred Feinberg
WILFRED FEINBERG
Circuit Judges

UNITED STATES COURT OF APPEALS
SECOND CIRCUIT

* * * *

[Title Omitted]

It is hereby ordered that the motion made herein by counsel for the appellants by notice of motion dated August 21, 1972, for leave to proceed in forma pauperis be and it hereby is granted.

/s/ Henry J. Friendly
HENRY J. FRIENDLY

/s/ J. EDWARD LUMBARD
J. EDWARD LUMBARD
Circuit Judges

/s/ Wilfred Feinberg
WILFRED FEINBERG

UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

(Argued February 28, 1973 Decided May 18, 1973.)

Docket No. 72-1972

In the Matters of

HENRY A. KOKOSZKA, FRANK O'BRIEN, and HERBERT E. SANDS,
BANKRUPTS-PETITIONERS

Before:

KAUFMAN, ANDERSON and MANSFIELD,
Circuit Judges.

Appeal by petitioners in bankruptcy from judgment affirming orders of the referee, which held that an income tax refund is "property" which passes to the trustee under § 70(a)(5) of the Bankruptcy Act, 11 U.S.C. § 110(a)(5), in the United States District Court for the District of Connecticut, Jon O. Newman, *Judge.*

Affirmed in part; reversed in part.

STUART BEAR, Esq., New Haven, Conn. (William H. Clendenen, Jr., Esq., David M. Lesser, Esq., Joanne Faulkner, Esq., and Frank Dineen, Esq., New Haven, Conn., on the brief), *for Appellants.*

(RICHARD BELFORD, Esq., New Haven, Conn., on the brief, *for Appellee Trustee in Bankruptcy.*)

ANDERSON, *Circuit Judge:*

The three appellants herein each filed separate individual voluntary petitions in bankruptcy, all of which raise the issue of whether or not, and to what extent, an income tax refund passes to the trustee in bankruptcy as property of the estate. In each case the petitioner had claimed the maximum number of deductions to which he was entitled on his tax withholding statement and in each case the refund was the only asset of the bankrupt estate.

Henry Kokoszka filed his petition and was adjudicated a bankrupt on January 5, 1972. On February 3, the referee ordered him to turn over the proceeds of his 1971 income tax refund to the trustee. After a motion to vacate the order was denied, Kokoszka petitioned for review in the District Court. In the meantime, he turned over the refund amount of $250.90 to the trustee to hold pending the determination of this matter, and he was given his discharge in bankruptcy on August 24, 1972.

Herbert Sands was adjudicated a bankrupt on February 4, 1970 and was ordered to turn over his 1969 tax refund to the trustee. Instead, Sands spent his refund of $201.97, and the trustee moved on March 12, 1971, to deny the discharge for this reason. Subsequent to that, the petitioner moved to vacate the turn-over order, but the referee denied the motion and denied the discharge. Sands then petitioned the District Court for review.

Frank O'Brien was adjudicated a bankrupt on April 30, 1970, and was ordered to turn over his 1969 refund of $136.00 to the trustee. He, too, failed to obey the order and the trustee moved to deny the discharge on March 18, 1971. The referee has not yet ruled on the trustee's motion, but he did deny O'Brien's motion to vacate the original turn-over order, and the petitioner sought review of that denial.

After consolidating the three cases, the District Court held that the tax refunds were property that passed to the trustee under § 70(a)(5) of the Act, 11 U.S.C. § 110(a)(5), and that the Consumer Credit Protection Act, 15 U.S.C. § 1671, et seq., did not require that the trustee return 75% of the refund to the petitioners. On these issues we affirm; however, we do remand Sands' case in order that the referee may exercise his discretion on whether or not to grant him a discharge in bankruptcy.

The primary point raised by this appeal is whether or not a tax refund is "property" which passes to the bankruptcy trustee under § 70(a)(5) of the Act.[1] The Ninth Circuit recently held that such a tax refund is not § 70 (a)(5) property, *In Re Cedor*, —— F.2d —— (9 Cir. Dec. 22, 1972); *aff'g on the opinion below*, 337 F. Supp. 1103 (N.D. Cal. 1972). *In Re Jones*, 337 F. Supp. 620 (D. Minn.) *leave to appeal denied* (8 Cir., May 14, 1971), *cert. denied*, 404 U.S. 1040 (1972), however, held that a refund does pass to the trustee and the same holding was implicit in *In Re Wetterhoff*, 453 F.2d 544 (8 Cir.), *cert. denied*, 409 U.S. 877 (1972), holding that, at the time of filing, the excess of accrued but unpaid wages over and above the portion exempt from attachment under state law, passed to the trustee.

The decision in the present case is governed in large part by two Supreme Court cases, *Segal* v. *Rochelle*, 382 U.S. 375 (1966), which held that a business generated

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[1] The pertinent parts of § 70(a)(5) of the Bankruptcy Act, 11 U.S.C. § 110(a)(5), read as follows:

> "(a) The trustee of the estate of a bankrupt . . . [shall] be vested by operation of law with the title of the bankrupt as of the date of the filing of the petition initiating a proceeding under this title . . . to all of the following kinds of property wherever located . . . (5) property, including rights of action, which prior to the filing of the petition he could by any means have transferred or which might have been levied upon and sold under judicial process against him, or otherwise seized, impounded, or sequestered . . . ."

It is undisputed that the refunds could have been transferred under Connecticut law at the time of the filing of the petition, *cf.*, *Segal* v. *Rochelle*, 382 U.S. 375, 381-385 (1966).

loss-carryback tax refund, which did not accrue until after the filing of the bankruptcy petition, was § 70(a)(5) property, and *Lines* v. *Frederick*, 400 U.S. 18 (1970), which held that vacation pay, accrued but unpayable at the time of filing, did not pass to the trustee.

For the purpose of considering what treatment should be given to the tax refunds in question here, the term "property" in § 70(a)(5) must be defined in terms of the purposes of the Bankruptcy Act, rather than by more traditional concepts, *Segal, supra,* at 379; *In Re Spanish Language Television,* 456 F.2d 159, 162 (9 Cir. 1972). Basically, the term "property" is given a generous construction in order to give creditors everything of value, including items where the enjoyment of value is postponed, *Segal, supra,* at 379; *In Re Robbins Converting Corp.,* 441 F.2d 1096, 1098 (2 Cir. 1971). The definition of property is limited, however, where the debtors are wage earners "whose sole source of income, before and after bankruptcy, is their weekly earnings," *Lines, supra,* at p. 20, and who, at the filing of their petitions in bankruptcy have wages, as such, or as vacation pay, accrued but not yet paid, and where "the minimal requirements for the economic survival of the debtor are at stake," *id.,* such wage payments are not "property" to be turned over to the trustee under § 70(a)(5). The purpose of this exception is to give the debtor a "new opportunity in life and a clear field for future effort, unhampered by the pressure and discouragement of preexisting debt," *Lines, supra,* at 1-20; *Local Loan Co.* v. *Hunt,* 292 U.S. 234, 244 (1934).

The test as to whether or not such items as accrued but unpaid wages are or are not "property" to be turned over to the trustee is whether the item is "sufficiently rooted in the pre-bankruptcy past and so little entangled with the bankrupts' ability to make an unencumbered fresh start that it should be regarded as 'property' under § 70(a)(5)," *Segal, supra,* 382 U.S. at 380.

There were two petitioners in *Lines,* both of whom had accrued vacation pay at the time of the filing of the petition, but neither could receive it until he either went on vaction or his employment was terminated. The one

petitioner, Frederick, worked for a manufacturing company which shut down for a week twice a year thereby forcing their employees to take a vacation. The other, Harris, could choose his vacation period, if he desired to take one.

If the vacation pay was held to be property of the estate, it would appear at first glance that Harris was in a somewhat better position that Frederick, because Harris was not forced to take a vacation and go without basic support. Nevertheless, he also was in a difficult position. If he took a vacation, he would have no income for that period; yet, if he did not, and he was laid off, he would not have the use of the pay upon termination for basic support while seeking new work.

Realizing that "[t]he function of their accrued vacation pay is to support the basic requirements of life for them and their families during brief vacation periods or in the event of a layoff," the Supreme Court held that this vacation pay was a specialized type of property that did not pass to the trustee because to hold otherwise would deny the debtor the new opportunity in life which the Bankruptcy Act intended to provide, *Lines*, *supra*, at 20.

What we have then in *Lines* is a very narrow exception to the general proposition that everything of value passes to the trustee, i.e., vacation pay which will become essential for basic week to week support in the future does not pass. Because a tax refund is not the weekly or other periodic income required by a wage earner for his basic support, to deprive him of it will not hinder his ability to make a *fresh* start unhampered by the pressure of preexisting debt. Therefore, the tax refund is § 70 (a)(5) property which passes to the trustee.

The petitioners have advanced several arguments, however, that bear some comment. First, they maintain that wages, as such, are a specialized type of property which does not pass to the trustee and that a tax refund is nothing more than a refund of over withheld wages. The problem with this argument is that when the Court in *Lines*, *supra*, at 20, or in other cases such as *Sniadach v. Family Finance Corp.*, 395 U.S. 337 (1969), speaks

of wages as a special type of property, it is referring to the periodic payments required to meet basic needs.[2] Just because some property interest had its source in wages, however, does not give it special protection, for to do so would exempt from the bankrupt estate most of the property owned by many bankrupts, such as savings accounts and automobiles which had their origin in wages.

The petitioners also argue that as wage earners they have come to rely upon the tax refund as an expected annual event and that to take it from them would deny them a fresh start in life. It was this reasoning that convinced the court in *In Re Cedor, supra,* at 1105, that tax refunds should not be § 70(a)(5) property, but we find it unpersuasive. Many people may come to rely upon such things as a Christmas Club account or year end dividends from stock ownership to give them a special source of income at certain times of the year, but this does not make such items immune from a turn-over order in bankruptcy. Permitting a bankrupt to retain his tax refund would not be giving him a "fresh start" to accumulate new wealth but a "head start" over others who had no such refund.

Finally, the petitioners argue that a tax refund should not be § 70(a)(5) property because such refunds will often be of no benefit to the creditors but will be used up in administration expenses.

We are concerned with the fact that, on the average, in all personal bankruptcy cases 41% of the assets of the estates are paid out of for trustees' fees and other administration expenses, D. Stanley & M. Girth, Bankruptcy: Problem, Process, Reform 91 (Brookings Institution 1971). Furthermore, nearly one case in five is one of only nominal assets, that is, a case where all of the assets in the estate are consumed in administration expenses, leaving nothing for creditors, Stanley & Girth, *supra,* at 87-88, 175.

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[2] We are fully aware that the petitioners in this case either spent or would spend their refunds for such needed items as health care, furniture and rent, but we do not see how the use of the money for what is characterized as "necessities" makes it any less § 70 (a)(5) property, *cf., Fuentes* v. *Shevin,* 407 U.S. 67, 90 (1972).

It is apparent why this happens in the small asset estates. Section 48(c)(1) of the Act, 11 U.S.C. § 76(c)(1), provides that a trustee can be compensated up to $150.00 plus expenses no matter how small the estate, and we have recently noted that in practice trustees are generally awarded the maximum fee, *In Re Schantz*, 390 F.2d 797, 800 (2 Cir. 1968); *see also*, Snedecor, Fees and Allowances in Straight Bankruptcy, 40 Ref. J. 26, 27 (1966). If that standard is applied to the cases currently before us, it can be seen that there will be nothing for creditors in the O'Brien estate and, at best, only a very small balance in the Kokoszka and Sands estates which might well be used up for other administration expenses, *cf.*, Stanley & Girth, *supra*, at 92, 173-195.

Clearly the purpose of the Bankruptcy Act was to benefit creditors and debtors, not trustees, *see*, *In Re Kingswood*, 343 F. Supp. 498, 504-05 (C.D. Cal.), *rev'd on other grounds*, —— F.2d —— (9 Cir. Dec. 22, 1972); *In Re Mc-Grath Mfg. Co.*, 95 F. Supp. 825, 829 (D. Neb. 1951). Therefore, there is no sense in taking a small sum from the bankrupt debtor, which he could well use to get started again, if there is to be no value to the creditors.

This does not mean, however, that all tax refunds should be held not to be § 70(a)(5) property, because a refund may be fairly large or only one asset among others. If a debtor is in a position where his non-exempt assets will be entirely eaten up by administration costs, leaving nothing for creditors, he can move the bankruptcy court for an order of abandonment,[3] *see In Re Mirsky*, 124 F.2d 1017 (2 Cir. 1942), *cert. denied*, 317 U.S. 638 (1942); *cf.*, *In re Ira Haupt & Co.*, 398 F.2d 607, 612-13 (2 Cir. 1968). See Calverley, Income Tax Refunds Due Wage Earners, 39 Ref. J. 8, 10-11 (1965), for a general discussion of the various abandoned practices of California referees for tax refunds. In moving for an abandonment, the debtor can present what evidence and

[3] A further benefit to a bankrupt debtor, if all assets are abandoned, is that a trustee need not be appointed which saves the petitioner $10 of the filing fee, *United States* v. *Kras*, —— U.S. —— (41 U.S.L.W. 4117, 4118, n. 2, Jan. 10, 1973).

arguments he may have to support his contention that it would not work an injustice to creditors to abandon the assets and not appoint a trustee. Whether or not to grant such a motion rests in the sound discretion of the Referee. He should grant the motion if it is reasonably clear that the assets, otherwise available for creditors, will be entirely consumed by trustee's fees and other administration expenses, that no creditor has shown that there was a likely opportunity for a trustee to recover additional assets, and that the absence of a trustee will not, under the circumstances, cast a substantial additional burden on the Bankruptcy Court.

The petitioners further argue, however, that even if a tax refund is § 70(a)(5) property, the trustee can take only 25% of it because of the Consumer Credit Protection Act's limitation on garnishment, 15 U.S.C. § 1671, et seq. That Act provides that no more than 25% of a person's aggregate disposable earnings for any workweek or other pay period may be subject to garnishment, 15 U.S.C. § 1673(a). The definitions of the key terms "earnings", "disposable earnings," and "garnishment" are set forth in the margin.[4]

The petitioners argue that a tax refund is "earnings" because it had its source in wages and that when it is returned to the taxpayer it is all "disposable earnings" because nothing is required by law to be withheld from the refund. Furthermore, they claim that the taking by the trustee is a "garnishment" because a bankruptcy pro-

[4] 15 U.S.C. § 1672 reads as follows:

"For the purposes of this subchapter:

(a) The term 'earnings' means compensation paid or payable for personal services, whether denominated as wages, salary, commission, bonus, or otherwise, and includes periodic payments pursuant to a pension or retirement program.

(b) The term 'disposable earnings' means that part of the earnings of any individual remaining after the deduction from those earnings of any amounts required by law to be withheld.

(c) The term 'garnishment' means any legal or equitable procedures through which the earnings of any individual are required to be withheld for payment of any debt."

ceeding is a legal or equitable procedure through which the earnings of an individual are withheld for payment of a debt.

Although this reasoning was adopted by the Ninth Circuit in *In Re Cedor, supra,* we do not follow it, but hold that a tax refund is not "earnings" for the purpose of § 1672 and, therefore, it is not protected by § 1673.

The intent of the Consumer Act was to make sure that wage earners were able to receive at least 75% of their take home pay in any one pay period so that they would have enough cash to meet basic needs. As a side effect, it was hoped that honest debtors, with this protection on their wages, would not be forced into bankruptcy, H. Rep. No. 1040, 90th Cong., 2d Sess., U.S. Code Cong. & Ad. News, 1962, 1977-79 (1968). It is clear, then, both from the language of the statute, §§ 1672, 1673, and the legislative intent, that "earnings" means periodic payments of compensation and does not pertain to every asset that is traceable in some way to such compensation. *See also,* 29 C.F.R. § 870.10(b): *In Re Kingswood, supra; cf. Lines, supra,* 400 U.S. at 20.

Petitioner Sands also appeals from the failure of the referee to exercise his discretion on whether or not to grant him a discharge in bankruptcy, even though he failed to obey the order to turn over his tax refund. The referee refused to consider a discharge, holding that § 14(c)(6) of the Bankruptcy Act, 11 U.S.C. § 32(c)(6),[5] mandated that he deny the discharge, if the bankrupt disobeyed a lawful order. The district court did not rule on the issue in this case, but in a similar case it remanded to the referee for him to exercise his discretion, *In Re Boudreau,* Bank. No. 36,601 (D. Conn. filed October 30, 1972).

Section 14(c) of the Act requires that a discharge be granted unless a bankrupt has done one of eight things,

[5] Section 14(c)(6) of the Bankruptcy Act, 11 U.S.C. § 32(c)(6) reads as follows:

> "(c) The court shall grant the discharge unless satisfied that the bankrupt has . . . (6) in the course of a proceeding under this title refused to obey any lawful order of, or to answer any material question approved by, the court; . . ."

among which is failure "to obey any lawful order of . . . the court," § 14(c)(6). The statute, however, does not state that a discharge *must* be denied for failing to obey an order, as the referee appears to have assumed.

As stated above, one of the primary purposes of the Bankruptcy Act is to give debtors a new chance in life and the various provisions of the Act must be read with this intent in mind, *Local Loan Co., supra,* 292 U.S. at 244-45; therefore Bankruptcy Courts must exercise their powers so that "substance will not give way to form" and "technical considerations will not prevent substantial justice from being done," *Pepper* v. *Litton,* 308 U.S. 295, 305 (1939). To this end, we have long held that the Act must be liberally applied toward the bankrupt applying for his discharge, *In Re Reisler,* 278 F. 618 (2 Cir. 1922); *see also, In Re Tabibian,* 289 F.2d 793, 795 (2 Cir. 1961).

Therefore the referee must exercise his discretion whether or not to grant a discharge, even when an order has not been followed. This position has strong support in the case law, *see, e.g. In Re Barbato,* 421 F.2d 1324, 1327 (3 Cir. 1970); *Jayne Meadows Travel Agency* v. *Dashiell,* 416 F.2d 1253, 1254 (9 Cir. 1969); *In Re Boudreau, supra; In Re Van Meter,* 208 F. Supp. 835 (S.D. Cal. 1962). The denial of a discharge can work a serious deprivation upon a debtor, and there are many circumstances where a bankrupt's disobedience may have been inadvertant or otherwise excusable. Moreover the denial of a discharge is not the only weapon available to the referee in order to enforce his orders as a recalcitrant petitioner can also be held in contempt, 11 U.S.C. § 69; *cf., In Re U. S. Hoffman Can Corp.,* 373 F.2d 622, 626 (3 Cir. 1967). This is not to be read, however, as minimizing the seriousness of the debtor's offense in disobeying a lawful order, nor do we suggest that a blatant violation should be condoned.

Therefore, before denying a discharge, the referee should weigh the detriment to the proceedings and the dignity of the court against the potential harm to the debtor if the discharge is denied. He should consider such factors as the intent behind the bankrupt's acts—

were they wilfull or was there a justifiable excuse; was there injury to the creditors; and is there some way that the bankrupt could make amends for his conduct. For example, in the present case, the referee might consider granting a discharge if the petitioner turns over to the trustee the amount of his refund check.

The decision of the District Court holding that the entire amount of the tax refunds is property belonging to the trustee in bankruptcy is affirmed; the case of petitioner Sands is remanded to the District Court for further proceedings consistent with this opinion.

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

At a stated Term of the United States Court of Appeals for the Second Circuit, held at the United States Courthouse in the City of New York, on the eighteenth day of May one thousand nine hundred and seventy-three.

Present: HON. IRVING R. KAUFMAN
HON. ROBERT P. ANDERSON
HON. WALTER R. MANSFIELD
Circuit Judges

72-1972

In the Matter of
FRANK O'BRIEN, APPELLANT

In the Matter of
HENRY KOKOSZKA, APPELLANT

In the Matter of
HERBERT E. SANDS, APPELLANT

Appeal from the United States District Court
for the District of Connecticut

This cause came on to be heard on the transcript of record from the United States District Court for the District of Connecticut, and was argued by counsel.

ON CONSIDERATION WHEREOF, it is now hereby ordered, adjudged, and decreed that the judgment of said District Court be and it hereby is affirmed in part and reversed in part and that the action as to appellant Herbert E. Sands be and it hereby is remanded to said District Court for further proceedings in accordance with the opinion of this court.

A. DANIEL FUSARO
Clerk

UNITED STATES OF AMERICA
SOUTHERN DISTRICT OF NEW YORK

I, A. DANIEL FUSARO, Clerk of the United States Court of Appeals for the Second Circuit, do hereby certify that the foregoing documents, numbered from SA, S1-8, OA, O1-6, KA, K1-7, SOK1-2, I-VI, inclusive, comprise the original record certified by the Clerk of the United States District Court for the District of Connecticut and a transcript of the proceedings had in this Court in the case of

In the Matter of
Henry A. Kokoszka, Bankrupt

as the latter remain of record and on file in my office.

[SEAL]

IN TESTIMONY WHEREOF, I have caused the seal of the said Court to be hereunto affixed, at the City of New York, in the Southern District of New York, in the Second Circuit, this twenty-third day of July in the year of our Lord one thousand nine hundred and seventy-three, and of the Independence of the said United States the one hundred and ninety-eighth.

A. DANIEL FUSARO
Clerk

by /s/ Vincent A. Carlin
Chief Deputy Clerk

SUPREME COURT OF THE UNITED STATES

No. 73-5265

HENRY A. KOKOSZKA, PETITIONER

v.

RICHARD BELFORD, TRUSTEE, ETC.

ON PETITION FOR WRIT OF CERTIORARI to the United States Court of Appeals for the Second Circuit.

ON CONSIDERATION of the motion for leave to proceed herein in forma pauperis and of the petition for writ of certiorari, it is ordered by this Court that the motion to proceed in forma pauperis be, and the same is hereby, granted; and that the petition for writ of certiorari be, and the same is hereby, granted.

December 10, 1973

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